

**LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

301 State House
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FISCAL IMPACT STATEMENT

LS 6303

BILL NUMBER: HB 1193

DATE PREPARED: May 3, 2001

BILL AMENDED: Apr 29, 2001

SUBJECT: Public Employee Benefits.

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FUNDS AFFECTED: ☒ **GENERAL**
☒ **DEDICATED**
FEDERAL

IMPACT: State & Local

Summary of Legislation: (CCR Amended) *Defined Contribution Plan:* The bill requires the State Personnel Department to adopt rules concerning: (1) the type and amount of leave that may be converted to a monetary contribution; (2) the conversion formula for valuing any leave that is converted; (3) the manner of employee selection of leave conversion; and (4) the vesting schedule for any leave that is converted. The rules adopted by the State Personnel Department must provide for a conversion rate under which the amount contributed on behalf of a participating employee for a day of leave that is converted is equal to at least 60% of the employee's daily pay on the date the leave is converted. The bill provides that the provisions may be implemented only if the Deferred Compensation Committee has received from the Internal Revenue Service any rulings or determination letters that the Committee considers necessary or appropriate. The bill also provides that the existing provisions establishing a Section 125 Cafeteria Plan program for unused leave time for state employees do not apply after the Defined Contribution Plan is implemented and the Deferred Compensation Committee has received from the Internal Revenue Service any rulings or determination letters that the Committee considers necessary or appropriate for the Defined Contribution Plan. It also provides that the Deferred Compensation Committee may use funds available under the plan to hire or contract with qualified attorneys, financial advisors, or other professional or administrative persons. The bill provides that the Deferred Compensation Committee may annually elect a chairperson and secretary. The bill also provides that the two members of the Deferred Compensation Committee who must be participants in the state employees' Deferred Compensation Plan may not serve for more than two consecutive three year terms. The bill authorizes a political subdivision that uses the state employees' Deferred Compensation Plan for its employees to participate in the state Defined Contribution Plan established under Section 401(a) of the Internal Revenue Code for the purpose of matching all or a specified portion of the political subdivision's employees' contributions to the Deferred Compensation Plan.

Purchase of Military Service Credit by PERF and TRF Members: The bill provides a procedure for members of the Public Employees' Retirement Fund (PERF) or the Indiana State Teachers' Retirement Fund (TRF) to purchase up to two years of military service credit to the extent service credit is not granted for that time

under existing PERF or TRF provisions. The bill requires a member to have at least ten years of creditable service in PERF or TRF before the member may use the military service credit. The bill also provides that the purchase of service credit provisions apply to members who retire after June 30, 2001.

Legislator's Retirement System: The bill requires the PERF Board to adopt rules for making loans to a participant in the legislator's retirement system.

Health Insurance for Retired Legislators: The bill also provides that certain elections by an employer concerning the payment of health insurance premiums and program eligibility may not be altered by the employer to the detriment of a former legislator.

Effective Date: (CCR Amended) Upon passage; July 1, 2001; July 1, 2002.

Explanation of State Expenditures: (Revised) *Defined Contribution Plan:* The bill would establish a Defined Contribution Plan under which state employees could annually convert excess accrued sick and vacation leave time into a monetary contribution to the Plan. Under the bill, the State Department of Personnel is required to provide for: (1) The type and amount of leave to be converted to monetary contributions; (2) the conversion formula; (3) the manner of employee selection of leave conversion; and (4) the vesting schedule for leave conversions. The bill also requires that the conversion rate be at least 60% of the employee's daily pay as of the date the leave is converted.

While the total impact of the bill is dependent upon the plan developed by the State Department of Personnel, the table below presents cost estimates for conversion of a vacation day and conversion of a sick day. These estimates are based on the current value of vacation and sick leave in excess of 30 days that has been accrued by state employees. The estimates assume that conversion of vacation days and sick days is limited to days an employee has accrued in excess of 30 days. For vacation days, this is done because state retirees are currently provided cash payment for up to 30 vacation days and the bill does not change this policy. The 30-day threshold is assumed for sick days for consistency. The estimates also assume a conversion rate of 60% and a 60% participation rate by eligible employees (the approximate participation rate for the state's Deferred Compensation Plan).

Conversion	Net Annual Cost With a 60% Conversion Rate and 60% Employee Participation
1 Vacation Day	\$270,000
1 Sick Day	\$230,000

The cost estimates are net amounts computed by subtracting from the converted value of a day the cost of fringe benefits attributable to that day. These fringe benefits would otherwise be paid if the employee were to utilize the day for leave purposes. A further offset of the cost of the bill potentially could be reductions in overtime costs in agencies where other employees must work overtime shifts to replace employees on leave. The Defined Contribution Plan may serve to reduce use of leave days, in particular unnecessary use of sick leave days, if employees prefer to convert such leave to the Plan instead of utilizing it. The actual impact of the bill is dependent upon the plan developed by the State Department of Personnel. Funding of this plan would come from the Personnel Services/Fringe Benefit Contingency fund for employees paid from the state General Fund, and other dedicated funds from which employees of some agencies are paid.

Background on the Current Section 125 Cafeteria Plan Program: The bill would eliminate the current Section 125 Cafeteria Plan Program provided the Defined Contribution Plan is implemented. Elimination of the Section 125 Cafeteria Plan Program would result in an annual saving of approximately \$700,000.

This estimate is based on state employees who retired with 10 or more years of creditable service in CY 2000. According to current statute establishing the Section 125 Cafeteria Plan Program, payment on behalf of an employee for unused leave time upon retirement is based on the hourly rate the employee was paid on the employee's retirement date times a fraction of the number of accrued, but unused, vacation, sick, and personal days. This fraction is determined by the following: (1) For an employee with at least 10 years but less than 15 years of creditable service, the fraction is 20%; (2) for an employee with at least 15 years but less than 20 years of creditable service, the fraction is 35%; and (3) for an employee with at least 20 years of creditable service, the fraction is 50%. The maximum amount that an employee is currently entitled to is \$5,000.

Legislator's Retirement System: The bill also provides that the PERF Board must adopt rules establishing procedures for making loans to a participant in the Legislator's Retirement System from the participant's employee contribution account and employer contribution account. It provides that the rules must comply with certain requirements under the Internal Revenue Code. There may be some administrative costs associated with this part of the proposal, but they are expected to be minimal.

Purchase of Military Service Credit by PERF and TRF Members: This bill can result in increased future payouts from PERF or TRF in certain situations, as described below.

Background: The bill provides that the purchase of the military service credits by members of PERF or TRF must be equal to the product of the following: 1) the member's salary at the time the member actually makes a contribution for the service credit; and 2) a rate determined by the actuary of the fund based on the age of the member at the time the member actually makes a contribution for service credit and computed to result in a contribution amount that approximates the actuarial present value of the benefit attributable to the service credit purchased. However, a couple of circumstances under which a member of PERF or TRF may wish to purchase military service credit and the potential impact to the funds are identified below.

1) If a member wanted to purchase military service credit (or any service credit), the actuary for the fund calculates the cost of that service based on the member's current salary, current PERF/TRF service earned, and the member's current age. This cost represents the full actuarial cost of the service at the time of the purchase (excepting any future Cost of Living Adjustments (COLAs) that may be awarded). In other words, if a member purchases the service credit on one day and then retires with benefits commencing the next day, there would be no immediate fiscal impact to either PERF or TRF. There also would be no immediate real gain to the member because the additional benefits received due to military service would be actuarially equivalent to the purchase price of the military service. This changes, however, once a COLA has been awarded. Since COLAs were not included in the purchase price, such a COLA would represent a real gain to the member and a fiscal impact to either PERF or TRF.

2) If the member purchases military service credit and continues employment, the member may also be able to benefit from the earlier purchase of service credit for a second reason. As the member continues employment, the member can expect increases in salary. These salary increases will increase the benefit the member can expect to receive at retirement. However, the purchase price of the military service was based on the member's salary **at the time of purchase** before any increases in salary. Any increase in the value of the member's benefit because of salary increases was not included in the purchase price, therefore

representing a real gain to the member and an impact to the fund.

Explanation of State Revenues:

Explanation of Local Expenditures: (Revised) *Purchase of Military Service Credit by PERF and TRF Members:* See Explanation of State Expenditures, above.

Explanation of Local Revenues:

State Agencies Affected: All; Public Employees' Retirement Fund; Teachers' Retirement Fund.

Local Agencies Affected: Local units with employees who are members of PERF or TRF.

Information Sources: Dan Novreske, State Budget Agency, 233-5707; Doug Todd of McCready & Keene, Inc., actuaries for PERF, 576-1508; Denise Jones of Gabriel, Roeder, Smith & Co., Inc., actuaries for TRF, 1-800-521-0498.